

SEATTLE CITY EMPLOYEES' RETIREMENT SYSTEM
Statement of Investment Policy and Procedures
Initially Adopted September 8, 1992
Last Revised September 4, 2003

I. STATEMENT OF PURPOSE

It is the purpose of the Seattle City Employees' Retirement System to provide adequate retirement and disability benefits to eligible municipal employees in a cost effective manner. This statement provides the framework within which the Retirement Board will manage the assets of the Retirement Fund.

II. INVESTMENT OBJECTIVES

Overall Performance Goals

It is the primary objective of the Seattle City Employees' Retirement System to achieve a long-term total annual rate of return, including dividends, interest, and capital appreciation which exceeds the assumed actuarial rate of return, currently 8% per year. A secondary long-term objective is to achieve a total annual return net of all investment management fees and expenses, which meets or exceeds a weighted average of the asset class benchmarks specified below, where the weights correspond to the Fund's strategic policy allocation.

Performance Goals By Asset Class

The performance objective of the portfolio's allocation to each asset class in which the Retirement Fund is invested shall be to achieve a total return net of fees and expenses which equals or exceeds the market indexes listed below over a full market cycle as defined by the System's consultant.

1. *Domestic Equities:* Russell 3000 Index
2. *International Equities:* Morgan Stanley Capital International (MSCI) EAFE Index
3. *Domestic Fixed Income:* Lehman Brothers Aggregate Bond Index
4. *Real Estate:* Russell NCREIF Index
5. *Alternative*
 - a. Hedge Funds EACM 100 Index
 - b. Private Equity: Wilshire Micro Cap Index
6. *Cash Equivalents:* One Month Libor

Manager Performance Measurement

Active investment managers in each asset class will be expected to outperform passive benchmarks related to both their asset class and their investment style by at least their management fees, and to

outperform the median manager in their investment style in the universe employed by the System's investment performance measurement consultant.

Risk and Diversification

In discharging its investment duties, the Board shall act with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims and shall diversify the investments of the employees' pension system so as to minimize the risk of large losses, all in accordance with RCW 35.39.060.

III. ASSET ALLOCATION

The asset allocation will be determined through appropriate studies undertaken by consultants retained by the Board of Administration. The allocation study will include all asset classes deemed prudent and appropriate by the Board. The Board, with the aid of the consultant, will determine the assumptions and criteria to be used in the asset allocation study. The following assumptions and criteria will be so determined:

1. The expected return from each asset category
2. The expected standard deviation of each asset category
3. The minimum and maximum percent to be invested in each asset category
4. The correlation relationship between the asset categories
5. The minimum acceptable return over a given time period
6. The net contribution as a percent of payroll
7. The expected payroll growth rate

The resulting asset allocation mixes will be reviewed by the Board with the consultant and an optimum selection made. The asset allocation study will be performed when circumstances so dictate. Appropriate adjustments to the existing portfolio will then be made in the most expeditious and appropriate manner.

As permitted by RCW Chapter 35.39 the assets of the Retirement Fund shall be diversified according to the specified target percentages:

STRATEGIC POLICY ALLOCATION

<u>Asset Class</u>	<u>Target</u>
<i>Cash and Cash Equivalents</i>	1 %
<i>Equities</i>	
Domestic	48 %
International	10 %
Alternative	10 %
<i>Fixed Income</i>	21 %
<i>Real Estate</i>	10 %
TOTAL	100 %

Cash equivalents shall be defined as any security in which the investment will last less than one week. All types of securities, direct or derivative, are permissible.

Equities are any equity interest in a corporation, partnership or other entity. All types of securities, direct or derivative, are permissible.

Fixed income is any debt obligation of a corporation, government or government agency. All types of securities, direct or derivative, are permissible.

Real estate is any interest in real property. All types of real estate investments, direct or derivative, are permissible.

On a quarterly basis, the Investment Committee (defined below) shall review actual portfolio holdings to insure compliance with the specified targets. Regular, systematic rebalancing of the portfolio back to the target percentages will be undertaken to insure attainment of the policy mix over the long term.

IV. ELIGIBLE INVESTMENTS

Investment Manager Guidelines

In accordance with the Investment Objectives stated above the Retirement Board shall provide each of the System's investment managers with a set of investment guidelines. These guidelines shall specify eligible investment, minimum diversification standards, and applicable investment restrictions necessary for diversification and risk control. Managers do not have authority to depart from their guidelines.

Economically Targeted Investments

Investment in securities of companies which promote a socially desired goal such as rewarding nondiscrimination and promoting local industry, will be given priority if the investment meets the goals of the Retirement System and if the resulting return on investment and related risk are comparable to other available investments in the same category.

Securities Lending

An agreement may be made with the System's bank custodian or other custodian retained by the Board to loan securities on behalf of the Retirement System. Securities that are loaned shall be fully collateralized in cash or other acceptable securities having at least 100% of the market value of the loaned security.

Commingled Group Trusts

Investments may be made in commingled group trusts. When the group trust is tax exempt, to meet the requirements of IRS Ruling 81-100 the declaration of trust governing each such group trust shall be deemed adopted as part of Seattle City Employees' Retirement System plan.

Derivatives

Investment in "derivatives" is permitted, however, leveraged derivatives or purchase of derivatives on credit is not permitted. Credit risk, market risk and legal risk will be determined by the Investment Committee to be appropriate before any investment is made in a derivative product. For these purposes derivatives shall be defined as securities whose return or market value is derived from another security or market index.

Currency Hedging

With the approval of the Investment Committee, international investment managers may hedge the currency risk associated with securities they manage for the Retirement System. Hedging may be accomplished through mechanisms approved by the Executive Director, including but not limited to currency futures contracts, currency purchases, and currency options. Approval to hedge must be obtained in advance and may be given orally or in writing. Managers need not obtain approval for each individual investment as long as the investment vehicle has been approved.

V. INVESTMENT PROCEDURES

- A. The Board shall have the power, but shall not be required to:
 - 1. Establish investment objectives
 - 2. Establish asset allocation goals

3. Establish ongoing investment strategy
4. Establish diversification limitations
5. Determine allocation of investable funds
6. Approve soft-dollar commitments
7. Approve special programs such as wholly-owned real estate investments
8. Monitor performance of funds
9. Establish subcommittees as necessary
10. Establish an Investment Advisory Committee as required by Washington State Law
11. Retain outside professional managers to manage various assets owned by the Retirement System
12. Retain outside professional consultants to provide performance review of investment managers, asset allocation studies and other projects, as the Board, in its discretion, deems appropriate
13. Establish a code of ethics to govern the action of the Retirement Board and Staff
14. Define eligible investment instruments

B. The Executive Director shall:

1. Carry out the policies, programs, and directives of the Board
2. Invest in-house assets subject to review by the Board
3. Provide for the timing, selection and execution of investment transactions in accordance with established policy
4. Have the authority to execute proxies
5. Prepare investment transaction summaries and statements of securities and cash.

C. The Board shall meet at least annually to review investment strategy and to review investment transactions and performance results.

D. The Board shall establish an Investment Committee. The Investment Committee will meet quarterly, or at the call of the Executive Director, to perform duties assigned to it. All Board members will be invited to attend Investment Committee meetings.

E. The Investment Committee shall make recommendations to the Retirement Board regarding asset allocation, investment opportunities, and the hiring or termination of investment managers. The Retirement Board will review and consider approval of the recommendations of the Investment Committee. The Investment Committee is authorized to increase or decrease funds of investment managers and shift funds between investment managers.

F. Distribution of Commissions

All bond and stock business shall be executed seeking best execution. “Best execution” means seeking to achieve the most favorable price and execution available, having in mind the System’s best interest, and considering all relevant factors. These factors include price, the size of the transaction, the nature of the market for the security, current market levels and trends, the reputation, experience and financial stability of the broker involved and the quality of service rendered by the broker in other transactions. Where feasible, the stock or bonds trades shall be distributed to brokerage firms where the Investment Committee has established a commission recapture / directed brokerage program.

G. Proxy Voting of Securities

Investment managers will be given the authority to vote proxies on behalf of the Retirement System. However, if the Executive Director determines that an investment manager’s voting policy, or any part thereof, does not serve the economic interests of the Retirement System, the Executive Director will report the situation to the Investment Committee and an alternate method of voting may be selected.

VI. SECURITIES CUSTODIAN

The Finance Director may cause any securities in which the City Retirement System deals to be registered in the name of a nominee without mention of any fiduciary relationship, except that adequate records shall be maintained to identify the actual owner of the security as registered. The securities so registered shall be held in the physical custody of the Finance Director, the designee of the Finance Director, or at the election of the designee and upon approval of the Finance Director, the Pacific Securities Depository Trust Company, Inc., or the Depository Trust Company of New York City or its designees.

With respect to the securities, the nominee shall act only on the direction of the Retirement Board. All rights to the dividends, interest, and sale proceeds from the securities and all voting rights of the securities shall be vested in the actual owners of the securities, or in the nominee.

VII. INVESTMENT MANAGER DISCRETION

1. Investment Managers, shall be available to meet at least annually with the Retirement Board or staff.
2. Investment Managers, following their agreements with the Retirement System, shall have the discretion to initiate purchases between meetings subject to the limitations imposed by availability of funds, and by the percentage goals established by the Retirement Board.

3. Investment Managers may sell any of the System's securities without prior Investment Committee approval.
4. Investment Managers shall supply securities appraisals and such other reports and analysis as the Board may from time to time reasonably request.
5. Investment Managers shall communicate with the Retirement Board and the Executive Director in writing whenever unusual, significant market activity occurs which could have an impact on the investment.

VIII. PERFORMANCE MEASUREMENT SERVICES

A performance measurement service will be retained to report quarterly on the market performance of the Retirement System investments. The report will compare the performance and risk levels of fixed and equity holdings to applicable indexes, and to other actively-managed portfolios.

IX. TRANSACTION AUDIT SERVICE

An audit service will be retained to review the transactions of the separately managed accounts held with the System's custodian. The audit service will perform a review based on criteria developed by the Investment Committee, including but not limited to: the review of all purchases and sales for proper pricing and proper recording, and interest and dividend income accrual reporting and subsequent collection.

X. INVESTMENT ADVISORY COMMITTEE

RCW 35.39.080 requires that any city operating an employees' pension system must appoint an Investment Advisory Committee consisting of at least three members who are considered experienced and qualified in the field of investments.

Duties of the Committee shall be as follows:

- (1) Make recommendations as to general investment policies, practices, and procedures to the Retirement Board including, but not limited to, asset mix, portfolio diversification, average maturity, portfolio risk level and rate of return;
- (2) Review the investment performance of the Retirement System;
- (3) Prepare a written report of its activities during each fiscal year. Each report shall be submitted not more than thirty days after the end of each fiscal year to the Retirement Board.
- (4) Review the Statement of Investment Policy and Procedures as adopted by the Retirement Board and make recommendations as to the content thereof.

- (5) Render advice to the Retirement Board relative to the desirability of and the procedure to retain investment advisors, performance measurement services, and bank custody of securities owned.
- (6) Select one Committee member to serve as Chairman at all meetings scheduled by the Committee.

No member of the Investment Advisory Committee is liable for the negligence, default, or failure of any other person or other member of the Committee to perform the duties of his or her office, and no member of the Committee may be considered or held to be an insurer of the funds or assets of the System nor shall any member be liable for actions performed with the exercise of reasonable diligence within the scope of his or her duly authorized activities as a member of the Committee. RCW 35.39.110.